

- *Economic growth remained strong in Q1-2022, led by the non-energy sectors.*
- *Inflation continued to be elevated in Q1-2022.*
- *Trade balance was in surplus in Q1-2022, supported by high energy prices.*
- *Credit to economy picked up in Q1-2022.*
- *State budget recorded a surplus in Q1-2022, despite slipping into deficit in March.*
- *Worsening global economic conditions pose downside risks to the economic outlook.*

Economic growth remained strong in Q1-2022, led by the non-energy sectors. The economy grew by 7 percent year on year (yoy) in March: the energy sector recorded 0.4 percent yoy growth while the non-energy sectors continued to grow robustly by 10.6 percent yoy. This brought the cumulative Q1-2022 growth to 6.8 percent yoy, with the non-energy sectors recording 10.3 percent growth. The expansion was broad-based in Q1-2022, led by non-oil/gas manufacturing (up 16.4 percent yoy) and services, with several sub-sectors picking up from pandemic lows, including hospitality (more than doubling yoy), transportation (up 20.5 percent yoy), ICT (up 14.7 percent yoy) and retail trade (up 4 percent yoy). Construction also picked up in February and March, and the sector grew by 5.6 percent yoy in Q1-2022. The revival was more modest in agriculture, which grew by 3.4 percent yoy. On the demand side, investment continued to contract, by 19 percent yoy in March, following a slight growth of 6 percent yoy in February. As a result, in Q1-2022, investment was down by 9.5 percent yoy, driven primarily by the drop in private foreign investment in the energy sector. Growth was supported by consumption, as indicated by the data on debit and credit card transactions (41.7 percent yoy growth in Q1-2022).

Inflation continued to be elevated in Q1-2022, driven by higher import prices and recovery in domestic demand. CPI inflation picked up in March, increasing by 1.1 percent month on month (mom) and reaching 12.1 percent annually. Food inflation rose by 1.5 percent mom, bringing annual food inflation to 16.6 percent. Both non-food and services inflation increased by 0.8 percent mom in March. As part of the measures to curb rising food inflation, the Cabinet of Ministers approved a resolution that introduced export permit system for essential food items.

The central bank kept the policy rate unchanged at 7.75 percent but stepped-up interventions to mop up liquidity. The Central Bank of Azerbaijan (CBA) acknowledged external inflationary pressures but anticipated that appreciating nominal effective exchange rate would have a dampening effect on inflation going forward. The CBA also reported some moderation in inflation expectations in Q1-2022, as compared to Q4-2021. Starting February, the CBA has significantly increased its note portfolio to reduce liquidity and, by end-

April, the portfolio amounted to AZN 770 million or 5.3 percent of the monetary base.

The trade balance was in surplus in Q1-2022, supported by high energy prices. Exports grew by 49.1 percent yoy in March, with energy exports expanding by 50.3 percent yoy and non-energy exports increasing by 40.8 percent yoy. Surging oil and natural gas prices drove growth in energy exports. Imports growth slowed in March to 3.9 percent yoy. Trade surplus in Q1-2022 rose to USD 5 billion, from USD 4 billion recorded in the first two months, and amounted to 28.6 percent of GDP.

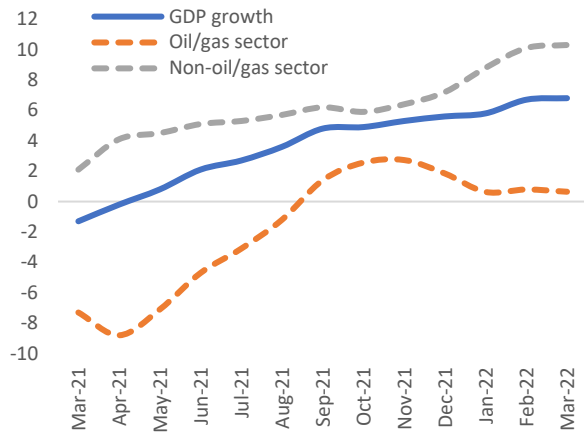
The manat remained stable at 1.7 AZN per USD amid some pick-up in FX demand. FX sales of the State Oil Fund (SOFAZ) rose by 7.6 percent yoy in April, following a 9.8 percent yoy increase in Q1-2022. The CBA reserves edged down by 0.3 percent mom in March and another 0.7 percent mom in April, but were still 11.3 percent higher in yoy terms (amounting to USD 7.1 billion by end-April). SOFAZ assets inched up by 0.5 percent in Q1-2022 as compared to end-2021, and reached USD 45.3 billion, or 83 percent of GDP, as stronger revenues from prices were offset by valuation losses.

The state budget balance was in surplus in Q1-2022, despite recording a small deficit in March amid higher budget spending. Budget revenues increased by 40 percent yoy in March (by 22.2 percent in Q1-2022), driven by an 80.2 percent yoy increase in energy revenues in March (due to higher SOFAZ transfers and higher taxes paid by energy companies). Non-oil/gas revenues also expanded by 5.9 percent yoy in March, supported by the robust tax collection of VAT, excises, and customs duties. Budget spending increased by 43.4 percent yoy in March (by 1.9 percent in Q1-2022), with current spending expanding by 29.3 percent yoy and capital spending doubling yoy in March. This increase in expenditure brought the state budget to deficit of AZN 196 million in March, but it remained in surplus of 4.6 percent of GDP for Q1-2022.

Bank lending continued to expand at a steady pace. Credit portfolio grew by 2.4 percent mom in March and by 5.2 percent when compared to end-2021. Expansion in lending was broad-based, with consumer lending increasing by 3 percent mom and business loans by 2.1 percent mom. Increase in bank deposits outpaced the rise in lending, recording 4.6 percent mom growth. Both manat and FX deposits rose, by 5.1 percent mom and 4.1 percent mom respectively, while dollarization rate stabilized at 51 percent. Bank profits jumped by 34.8 percent mom in March and cumulatively by 16.9 percent yoy in Q1-2022.

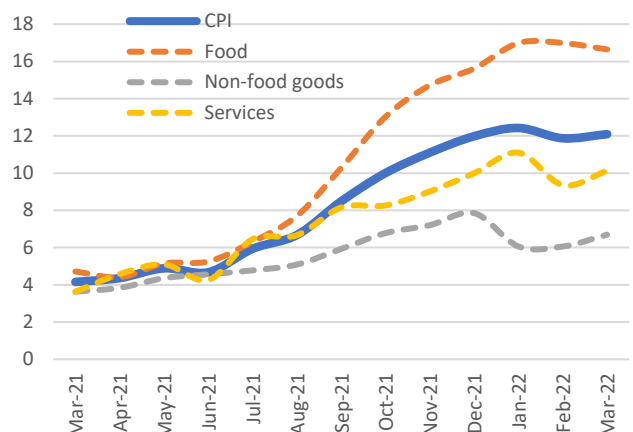
Global economic conditions continued to deteriorate by early May, posing downside risks to economic outlook. The war in Ukraine, COVID-19 lockdowns in China, and tightening of the global financial conditions are expected to weigh on global and regional activity and contribute to rising commodity prices (including food prices). This, in turn, raises uncertainty and could weigh on Azerbaijan's economic outlook going forward.

Figure 1. Economic growth remained strong in Q1-2022.
(ytd, %)



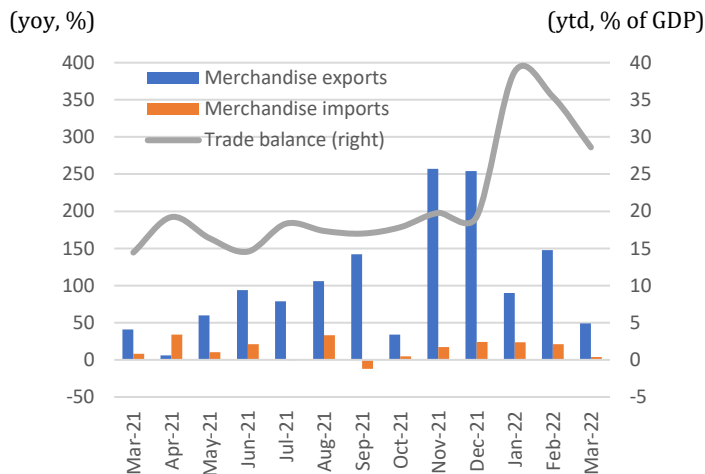
Source: State Statistics Committee

Figure 2. Inflation continued to be elevated in Q1-2022.
(yoy, %)



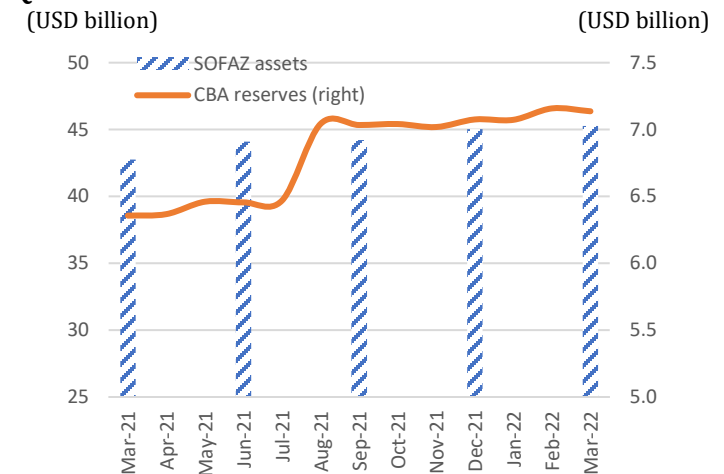
Source: State Statistics Committee

Figure 3. Trade surplus was solid in Q1-2022.



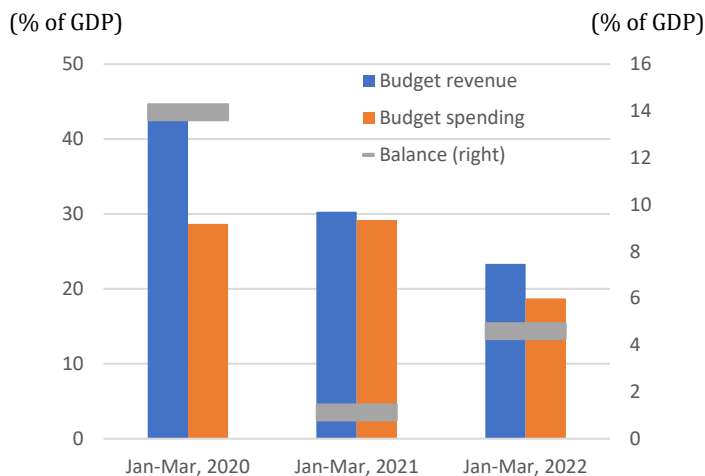
Source: State Customs Committee

Figure 4. CBA reserves and SOFAZ assets were stable in Q1-2022.



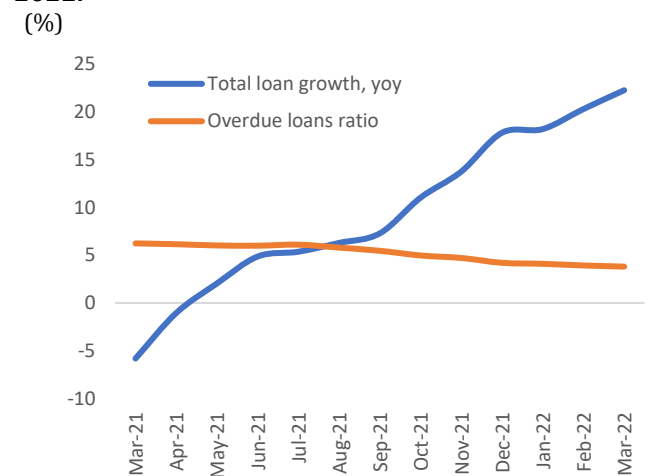
Source: Central Bank of Azerbaijan

Figure 5. State budget recorded surplus in Q1-2022.



Source: Ministry of Finance

Figure 6. Credit to economy remained healthy in Q1-2022.



Source: Central Bank of Azerbaijan